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DOE PASS TO GPERSON AND JHART
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E.O. 12958: DECL: 05/14/2017
TAGS: EPET ENRG EIND SA
SUBJECT: DOW AND SAUDI ARAMCO SIGN MOU FOR $20 BILLION PETROCHEMICAL PLANT

Classified By: ECONOMIC COUNSELOR ROBERT SILVERMAN
FOR 12958 1.4 B, D, AND E

Summary

¶1. (C) On May 12, US firm Dow Chemical's CEO Andrew Liveris and Saudi Aramco's President and CEO Abdullah Jum'ah signed a detailed Memorandum of Understanding for a major petrochemical facility, the "Ras Tanura Integrated Project" (RTIP), the cost of which will likely reach more than $20 billion. The firms plan to construct the plant at Ras Tanura in Saudi Arabia's Eastern Province, with operations integrated into those of the existing Ras Tanura Refinery and Ju'aymah gas processing plant. Dow told Dhahran Consulate officers that the projected plant will employ about 4,000 workers in the operational phase, and up to 50,000 during peak construction. Once completed, the plant will be the largest foreign investment in Saudi Arabia's energy sector. Dow officials described the envisaged facility as the largest current petrochemical project under construction in the world, and the largest joint venture project in the history of Dow. The plant will be a key component in SAG policies to increase the size of its gas sector, diversify its economy into gas-based manufacturing, and generate employment for a growing Saudi population.

Commitments within the New MOU

¶2. (C) On May 12, Consul General Kincannon, Pol/Econ Off Randolph, and FCS Commercial Specialist Malas met with a Dow delegation consisting of John Dearborn, President for the Middle East, India, and Africa; Mike Gambrell, Executive Vice President for Plastics; and Louis Vega, Director of Public Affairs. According to the Dow delegation, the May 12 MOU states Dow and Saudi Aramco have agreed to:

--Study the project further to make sure that it is economically viable;

--Negotiate definitive and ancillary agreements; and
--Conduct a feasibility study which will take approximately 24 months to complete.

Dow's Product Mix Key to Winning Bid;
Aramco Unimpressed with SABIC Efforts

¶3. (C) The delegation told CG Kincannon that 10-12 companies initially bid on the project, but Dow, Saudi national petrochemical company SABIC, and German-based BASF were the finalists. Dow emerged the final winner. For Dow's part, CEO Liveris encapsulated the project's attraction: "a long-term, secure, and reliable feedstock."

¶4. (C) Saudi Aramco's Senior Vice-President of Finance al-Othman recently provided some insight into the bidding process when he told CG Kincannon that Saudi Aramco "is frustrated with SABIC." Saudi Aramco perceives SABIC as "lazy" in continuing to focus on the export of bulk raw petrochemicals, and failing to push into tertiary industries. Al-Othman indicated Dow's wide product mix and consistent push for a deal in the Middle Eastern region gave them the needed edge over SABIC and BASF.

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Integrated Operations To Employ 4000; 50,000 Workers in Construction; Dow Allocated Most Feedstock
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¶5. (SBU) The scope of the proposed project is vast. The Dow delegation estimated that when operational, the plant will employ about 4,000 people. At peak construction times, it will employ up to 50,000 workers.

¶6. (C) Dow indicated the new plant would be operationally integrated with the existing Ras Tanura Refinery and the Ju'aymah gas processing plant. Dow Director Vega generally concurred with press reports that RTIP's feedstock will consist of 550,000 barrels of oil equivalent per day from those plants. He added that Dow had received an allocation letter covering most, but not all, of the feedstock. Vega stated to Energy Attache that Dow and Saudi Aramco have reached agreement on the base streams, but not specific sources, for the feedstock. The plant will utilize both oil and gas as feedstock. Saudi Aramco CEO Ju'mah indicated in the press conference that the plant will start operations in 2012-2013, and produce 4.5 million tons of basic chemicals and 7 million tons of derivative plastics and chemicals per year.

¶7. (U) Dow has publicly stated that the core units in the plant are an ethane and naptha cracker, a catalytic cracking unit, and an aromatics unit to convert sour Saudi crude to high value plastics. Dow Director Vega confirmed press reports for Energy Attache that the project would feature 30 downstream process units and produce more than 300 different products, including etheylene, propylene, aromatic and chlorine derivatives. These petrochemicals could provide inputs for manufacturing numerous products, including water purification chemicals, pharmaceuticals, plastics, piping, carpeting, paint, coatings and sealants, electronics, automotive parts, personal healthcare items, furniture, and shoes.

Looking Ahead: A Conversion Park
for Industrial Manufacturing

¶8. (C) In line with the SAG's goal to expand Saudi manufacturing, Dow Director Vega outlined Dow's vision for the next phase of the project: an integrated facility for conversion of petrochemical products into industrial goods. Dow has such a facility in Germany, where it substantially minimizes transport and storage costs. Vega noted most of the RITP's products would be in liquid form which could piped "next door" to manufacturing facilities. Dow supports such an arrangement because it delivers them a "captive customer base," while downstream manufacturers would enjoy the advantages of a reliable and efficient feedstock. Vega explained the SAG strongly supports such an initiative; the petrochemical industry creates seven indirect ("downstream") jobs for every one direct job, and the SAG is anxious to retain this employment in-country.

¶9. (C) Vega told us the SAG is not yet discussing the conversion plant option publicly, and has expressed concern to Dow regarding the Ras Tanura community's willingness to accept a chemical plant and additional associated facilities. He noted the SAG believes Ras Tanura community is accustomed to oil facilities, but not yet familiar with the concept of a chemical plant in their midst. There are also concerns with congestion in the Ras Tanura area.

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Dow Soon to Launch Public Affairs Campaign in KSA;
Dow Concerned with Charitable Contributions
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¶10. (C) To introduce the citizens of Saudi Arabia to Dow, and to address community concerns with construction of a major chemical plant, Dow soon plans to launch its "human element" public affairs campaign in Saudi Arabia. The campaign will emphasize Dow's themes of leadership in customer service, environmental stewardship, sustainability, and charitable outreach. Given USG concern with specific Saudi charitable organizations, Director Vega also requested US Mission assistance in determining which Saudi charities might be appropriate partners for Dow.

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Petrochemical Expansion in Line with SAG Drive for
Growth in Natural Gas, Diversification, Employment
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¶11. (U) Prior to the Dow announcement, on May 10, Minister of Petroleum and Mineral Resources Naimi announced a much-publicized expansion of Saudi Arabia's gas sector. He forecast a 40 percent increase in domestic gas demand from 2006 to 2012, and emphasized the need to further open the natural gas sector to foreign investment to meet this demand. Minister Naimi also stated the SAG plans to invest $70 billion in petrochemicals through 2015 to move from the number 10 to number 3 producer in the world, increase petrochemical production from 60 million tons to 100 million tons by 2015, and double the number of petrochemical products. The RTIP advances key SAG policies on a number of fronts: expanding the natural gas sector, moving up the petroleum value chain into more complex manufacturing processes, and generating significant employment for Saudi citizens. In a statement issued at the MOU signing, Saudi Aramco CEO Jum'ah also highlighted the role of the plant in

expanding the national economic base and promoting economic diversification.

Financial Structure; Dow Dismisses Concerns with Project's High Costs
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¶12. (C) During the meeting with CG Kincannon, the Dow delegation highlighted their experience in joint venture operations, stating they operate more than 80 such projects around the world. The Dow delegation stated Dow and Saudi Aramco would contribute equally towards the estimated $20 billion USD investment. Final costs will depend partly on the number of processing units, currently about 30. The project's debt/equity ratio will be 70/30. The delegation indicated the project will start off with an initial equity infusion of about $2 billion USD, with a larger amount from debt. Dow CEO Andrew Liveris stated during the press conference, "The investment is Dow's largest in the region, and our biggest joint venture. It is the largest proposed joint venture in our 110-year history."

¶13. (SBU) Public Affairs Director Vega dismissed speculation in the press that escalating costs in the petroleum sector could endanger the project, stating that "yes, while costs in the sector have increased, Dow realized it could do more on the project." He explained that a decision to add processing units to increase plant capacity was responsible for most of the increase in the proposed budget, rather than rising costs in the energy supply chain.

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Initial Public Offering Demand Muddies Financial Waters, Dis-pleases Dow and Saudi Aramco
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¶14. (C) Dow confirmed reports there will be an initial public offering (IPO) for the 30% of the

project at cost to the Saudi public. (Note: The SAG has frequently mandated IPOs for major projects to spread proceeds from the oil revenues, and promote greater Saudi participation in an "ownership society." End note.) However, Dow remains concerned the IPO could constitute a sizable "value leak," and is concerned that the Saudi stock market lacks a strong regulatory process. Dow continues to argue for a later IPO, once the project has a track record and has begun to create value for shareholders.

¶15. (C) In a separate meeting, Saudi Aramco's Senior Vice-President of Finance al-Othman told CG Kincannon that Saudi Aramco shared Dow's view that an IPO should come much later in the process. He described the SAG's earlier policy of consistently pushing for early IPOs, but said it has become more cautious after the 2006 stock market crash. Instead, the SAG is now coming around to a view that mature projects with solid earnings make a better offering than a greenfield project which has not booked any revenue. Al-Othman took a more favorable view than Dow did on the current state of Saudi stock market regulation, noting that while many regulations were not yet codified in law, the SAG's "guidelines" were quite good, and close to American practices. He particularly highlighted a recent provision that holds the director of a company civilly and criminally liable if he is found negligent in not acting in the best interests of all shareholders.

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Moving Ahead: Four US Firms Shortlisted for FEED;

Three Would Base Work in UK or Canada
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¶16. (C) The next major phase of the RTIP is to conduct the front end engineering and design (FEED) work. On April 29, Aramco and Dow announced four US firms shortlisted to carry out the FEED study: KBR, Fluor, Foster Wheeler, and Bechtel. Unique among the four firms, KBR is planning to bid the project out of Houston, but has contacted our Foreign Commercial Service to express concern the US visa situation may adversely impact their bid. The other three firms are planning to bid either from their London or Calgary offices.

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Visa Concerns Drive Most Work to Dubai, Europe
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¶17. (C) President Dearborn underscored Dow's serious concerns with their ability to obtain US visas for Saudi staff in a timely manner, and how this is impacting their decision on where to locate staff for the RITP project. Most of the FEED work will be carried out in Dubai. Dow is not yet prepared to re-locate their staff to Saudi Arabia yet, but they plan to establish a legal entity in the KSA soon. Due to visa concerns, Dow also plans to carry out all engineering training in Europe.

Comment
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18 (C) Yesterday's agreement was the announcement of a two year engagement, one which will hopefully lead to a happy marriage. The RITP project is a rare recent example of a US firm landing a major Saudi Aramco project. Instead, large-scale projects in past years have gone to Chinese, Russians, Italian, and Dutch interests (the Rub al-Khali joint venture gas projects) and others to the Japanese (PetroRabigh Refining and Petrochemical plant). Nonetheless, Dow and its potential FEED contractors have made it clear that at present, significant value from this multi-billion

project will not flow to the US, due to concerns with obtaining visas for its staff. Mission hopes appropriate measures can be taken to ensure Dow is able to source some work for the Ras Tanura Integrated Project from its US offices, rather than relocate this work elsewhere.

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